

STATE OF MICHIGAN  
BEFORE THE MICHIGAN PUBLIC SERVICE COMMISSION

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In the matter of the application of	)	
<b>Consumers Energy Company</b> for	)	Case No. U-16045-R
the reconciliation of Power Supply	)	
Cost Recovery costs and revenues	)	
<u>for the calendar year 2010.</u>	)	

**NOTICE OF PROPOSAL FOR DECISION**

The attached Proposal for Decision is being issued and served on all parties of record in the above matter on June 22, 2012.

Exceptions, if any, must be filed with the Michigan Public Service Commission, 4300 West Saginaw, Lansing, Michigan 48917, and served on all other parties of record on or before July 13, 2012, or within such further period as may be authorized for filing exceptions. If exceptions are filed, replies thereto may be filed on or before July 27, 2012.

**The Commission has selected this case for participation in its Paperless Electronic Filings Program. No paper documents will be required to be filed in this case.**

At the expiration of the period for filing exceptions, an Order of the Commission will be issued in conformity with the attached Proposal for Decision and will become effective unless exceptions are filed seasonably or unless the Proposal for Decision is reviewed by action of the Commission. To be seasonably filed, exceptions must reach the Commission on or before the date they are due.

MICHIGAN ADMINISTRATIVE HEARING  
SYSTEM  
For the Michigan Public Service Commission

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Sharon L. Feldman  
Administrative Law Judge

June 22, 2012  
Lansing, Michigan

STATE OF MICHIGAN  
MICHIGAN ADMINISTRATIVE HEARING SYSTEM  
FOR THE MICHIGAN PUBLIC SERVICE COMMISSION

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<u>for the calendar year 2010.</u>	)	

**PROPOSAL FOR DECISION**

**I.**

**PROCEDURAL HISTORY**

This Proposal for Decision (PFD) addresses Consumers Energy Company's (Consumers) March 31, 2011 filing seeking to reconcile its Power Supply Cost Recovery costs and revenues for calendar year 2010.

The company's filing identifies 2010 total system power supply costs of \$1,723,092,482 and total revenues of \$1,742,777,535, resulting in a net overrecovery of \$19,685,054. The company also identifies a prior period (2009) underrecovery of \$34,378,062, for a cumulative net underrecovery of \$14,801,006 including interest through December 2010. The filing was accompanied by the prefiled testimony of Richard T. Blumenstock, Thomas P. Clark, Laura M. Collins, Steven C. Foster, David B. Kehoe, Dee Dee A. Mortimer, and David F. Ronk, Jr.

At the May 26, 2011 prehearing conference, the company and Staff appeared, and the following parties appeared and were granted intervention: Michigan Environmental Council (MEC), the Attorney General, Midland Cogeneration Limited Partnership, the Association of Businesses Advocating Tariff Equity (ABATE), the Michigan Community Action Agency Association (MCAAA), and the Biomass Merchant Plants (BMPs). The BMPs include Cadillac Renewable Energy, LLC; Genesee Power Station LP; Grayling Generating Station LP; Hillman Power Company, LLC; TES Filer City LP; Viking Energy of McBain, LLC; and Viking Energy of Lincoln, LLC. The parties agreed to a schedule.<sup>1</sup>

On July 15, 2011, the BMPs filed the testimony of Timothy R. Schimke, William (Bill) E. Smith, Edward P. ("Ted") Barrett, Jr., Philip E. Lewis, Keith A. Mulka, Robert Joe Tondu, Neil R. Taratutta, Donald Adams, and Thomas V. Vine. On December 8, 2011, MEC filed testimony from its consultant, George E. Sansoucy; MCAAA filed the testimony of William A. Peloquin, the Attorney General filed the testimony of Richard F. Hasselman, and Staff filed the testimony of Jay Gerken. Consumers filed rebuttal testimony from Mr. Blumenstock, Mr. Clark, Mr. Foster, Mr. Ronk, and Brian D. Gallaway on January 11, 2012. Staff filed the rebuttal testimony of Jesse J. Harlow.

At the hearing on February 9, 2012, 3 witnesses (Messrs. Blumenstock, Gallaway, and Foster) appeared and were cross-examined, while the testimony of the remaining 19 witnesses was bound into the record by agreement of the parties, without the need for the witnesses to appear. On February 16, 2012, the ALJ issued a ruling approving transcript revisions, by agreement of all parties, to correctly state the amount

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<sup>1</sup>The schedule was subsequently adjusted to extend the Staff and intervenor filing date by one day, by agreement of the parties.

of NOx allowance costs TES Filer City LP (TES) is seeking. Following the established schedule, Consumers, Staff, the BMPs, MEC, MCAAA, and the Attorney General filed briefs on March 8, 2012, and reply briefs on March 22, 2012.

The evidentiary record is contained in 543 transcript pages, and 62 exhibits. By agreement of the parties, official notice was also taken of identified portions of the testimony of three of the witnesses (Messrs. Ronk, Gallaway, and Foster) given in prior cases.<sup>2</sup> A brief overview of the record and positions of the parties is presented in section II below, and a discussion of each of the issues in section III.

## II.

### **OVERVIEW OF THE RECORD AND POSITIONS OF THE PARTIES**

#### Consumers

Ms. Mortimer presented the company's PSCR reconciliation calculations.<sup>3</sup> Her Exhibit A-16 shows monthly PSCR revenues and costs for 2010, while the interest calculations are presented in Exhibit A-17. She testified that four categories of sales are considered non-PSCR sales, including sales to nonjurisdictional wholesale customers, Grand Rapids special contract sales, Rate GSG-2 sales, and sales to other special contract customers whose costs are excluded.

Ms. Collins testified regarding the company's proposed roll-in of the underrecovery into the 2011 PSCR factor calculation, citing the Commission's December 21, 2006 order in Case No. U-15001.<sup>4</sup>

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<sup>2</sup> See 2 Tr 430-431.

<sup>3</sup> Ms. Mortimer is a Senior Accounting Analyst for Consumers. Her testimony is transcribed at Tr 43-50.

<sup>4</sup> Ms. Collins is a Senior Rate Analyst for Consumers. Her testimony is transcribed at Tr 22-24.

Mr. Foster testified regarding the coal, oil, and natural gas costs incurred by the company during 2010. His Exhibit A-6 shows the as-burned volumes and cost of coal compared to the plan projections. He testified that total coal volumes were 8% below projected levels, with higher transportation costs increasing western contract coal costs above plan case projections, both higher transportation and higher commodity costs increasing eastern contract coal costs above plan case projections, and higher commodity prices increasing spot coal costs as well. His Exhibit A-7 compares the actual oil and gas burn volumes and costs for the plan year to plan case forecasts. He testified that the total oil and gas costs were less than projected because the overall level of generation for the oil and gas units was less than projected, with lower costs for No. 6 fuel oil below projections due to oil inventory carried over from 2009, and lower natural gas costs due to lower than expected market prices.

Mr. Blumenstock testified regarding the company's transportation costs, and regarding the company's contracts to provide natural gas supply to the Zeeland plant.<sup>5</sup> He testified that the company used two gas management services agents to supply gas to Zeeland, and that the agents, BP and EDF, were selected through a competitive bidding process.<sup>6</sup> He presented Exhibits A-1 and A-2 to support his testimony.

Mr. Kehoe testified regarding outages at the company's generating plants.<sup>7</sup> He identified both short duration and longer duration planned outages during 2010, and

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<sup>5</sup> Mr. Blumenstock is Director of Fossil Fuel Supply for Consumers. His testimony, including rebuttal and cross-examination, is transcribed at 324-411.

<sup>6</sup> As discussed in more detail below, the agents in 2010 were BP Canada Energy Marketing Corporation (BP) followed by EDF Trading North America, LLC (EDF).

<sup>7</sup> Mr. Kehoe is Director of Staff for the Electric Generation staff of Consumers; his testimony is transcribed at 2 Tr 26-41.

also presented comparisons of the company's outage rates in 2010 to outage rates in 2009, and to national GADS data over one and five-year time frames.

Mr. Kehoe also testified regarding NO<sub>x</sub>, SO<sub>2</sub>, and urea expenses. He identified 2010 actual NO<sub>x</sub> allowance expenses of \$73,815, explaining that the allowance expenses were higher than projected in the plan case because the plan case estimate excluded potential compensation to the co-owners of the Campbell unit 3. He also identified SO<sub>2</sub> credits of \$53,686, and urea expenses of \$1,345,064, below the plan case projection due both to lower urea costs and to outages reducing utilization. He supported his testimony with Exhibits A-8 through A-15.

Mr. Clark testified regarding the calculation of the PSCR cost component of renewable energy under 2008 PA 295, referred to as the "transfer cost".<sup>8</sup> In his calculations, presented in Exhibits A-3 through A-5, capacity, off-peak energy, and on-peak energy are priced separately for each of six renewable energy purchase power agreements, while on-peak energy is used exclusively to determine the transfer cost of the company's Experimental Advanced Renewable Program. He testified that the transfer prices used for capacity and energy in these calculations are based on values approved by the Commission at the time the contracts were approved. Exhibit A-3 shows the calculation of the total 2010 transfer cost of \$1,255,213, adjusted to exclude energy delivered in 2009 but booked in 2010, while Exhibit A-5 shows that the average transfer price used is \$57.42 per MWh. He further testified that for each contract, the transfer cost was less than the total contract payments, which are shown on Exhibit A-3.

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<sup>8</sup> Mr. Clark is a General Engineer in the Transaction and Resource Planning Section of Consumers' Energy Supply Department. His direct and rebuttal testimony is transcribed at 82-107.

Mr. Ronk testified regarding the company's purchased power costs, including allocation of costs to the company's renewable resource fund, MISO market settlement costs, third-party sales, and reduced dispatch arrangements.<sup>9</sup> He presented Exhibits A-18 through A-24. His Exhibit A-18 summarizes the company's purchased, interchanged and renewable power transactions for 2010, reflecting Mr. Clark's transfer price calculations. Referencing the purchased power contracts identified in his Exhibit A-20, Mr. Ronk also indicated that two agreements relating to the company's Experimental Advanced Renewable Program had not been approved by the Commission, but testified that the company is not seeking to recover capacity charges associated with these agreements at this time.

His Exhibit A-21 presents a comparison of the actual purchases during 2010 to the plan projections. He testified that the amount of energy required to serve customers in 2010 was 3.8% more than the forecast, with an increase in purchased power of 11.85% primarily attributable to an increase in purchases from the MCV, as well as an increase in MISO market purchases. The company's net settlement with MISO for 2010 is summarized in Exhibit A-23.

Mr. Ronk also testified as to how costs associated with the company's renewable resources program (the "Green Power" or "Green Generation" Program) approved in Case No. U-13843, were treated in the PSCR reconciliation, indicating that these costs do not impact the PSCR cost per kWh. He also explained that the company did not enter additional PPAs for this program in 2010, but did extend a PPA originally scheduled to expire during the year.

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<sup>9</sup> Mr. Ronk is Director of Electric Transactions and Resource Planning for Consumers. His direct and rebuttal testimony is transcribed at 2 Tr 52-81.

## BMPs

The BMPs presented the testimony of the plant managers for each of the plants, as well as testimony from the individuals who procure fuel for the plants, if the plant managers do not have that responsibility. These witnesses generally testified to the reasonableness and prudence of the company's fuel and variable operations and maintenance expenses. Mr. Schimke testified as plant manager for Cadillac Renewable Energy, LLC to both the fuel procurement practices and total costs eligible for recovery, and presented Exhibit BMP-3.<sup>10</sup> Mr. Smith testified as plant manager for the Genesee Power Station Limited Partnership, and presented Exhibit BMP-4.<sup>11</sup> Mr. Barrett, sole member of Controlled Performance LLC and general manager of Mid-Michigan Recycling, L.C., testified to the fuel procurement practices for the Genesee plant, presented Exhibits BMP-12 and BMP-13, and also sponsored the summary exhibits BMP-1 and BMP-2 on behalf of the BMPs collectively.<sup>12</sup> Mr. Lewis testified as plant manager for the Grayling Generating Station Limited Partnership, and presented Exhibit BMP-5.<sup>13</sup> Mr. Mulka testified as plant manager for Hillman Power Company, LLC and presented Exhibit BMP-6.<sup>14</sup> Mr. Taratutua testified as plant manager for Viking Energy of Lincoln, LLC, presenting Exhibit BMP-8,<sup>15</sup> while Mr. Vine testified as plant manager for Viking Energy of McBain, LLC, presenting Exhibit BMP-9.<sup>16</sup> Mr. Adams, Regional fuel manager for Viking, testified to the reasonableness and prudence of the fuel

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<sup>10</sup> Mr. Schimke's testimony is transcribed at 2 Tr 114-129.

<sup>11</sup> Mr. Smith's testimony is transcribed at 2 Tr 130-142.

<sup>12</sup> Mr. Barrett's testimony is transcribed at 2 Tr 143-161.

<sup>13</sup> Mr. Lewis's testimony is transcribed at 2 Tr 162-178.

<sup>14</sup> Mr. Mulka's testimony is transcribed at 2 Tr 179-195.

<sup>15</sup> Mr. Taratuta's testimony is transcribed at 2 Tr 229-241.

<sup>16</sup> Mr. Vine's testimony is transcribed at 2 Tr 242-253.

procurement practices for both Viking plants.<sup>17</sup> Mr. Tondou testified as owner of TES, testifying to the company's fuel procurement and operating costs as presented in Exhibit BMP-7, including the company's claim for recovery of NOx and SO<sub>2</sub> allowance costs as reflected in this exhibit and Exhibit BMP-2, and additionally presenting Exhibits BMP-10 and BMP-11 in support of that claim.<sup>18</sup>

#### Attorney General

Mr. Hasselman testified regarding the transfer price used in the reconciliation, contending that the transfer price used in the reconciliation should be based on actual expenses rather than projected prices used in plan and contract-approval cases.<sup>19</sup> By actual expenses, Mr. Hasselman explained that the transfer prices should reflect the actual expense that would have resulted had Consumers purchased energy at the economically-dispatched Locational Marginal Price or "LMP" rather than the renewable energy purchased. He testified that transferring costs above the actual economic dispatch cost to PSCR costs evades the rate caps set by section 45 of Act 295, artificially inflating PSCR expense and reducing the incremental cost of compliance. He acknowledged that his recommendations conflict with the Commission's decision in Case No. U-15675-R, but pointed out that the Attorney General has appealed that decision.

The Attorney General also presented Exhibit AG-1, containing stipulations regarding the BMPs.

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<sup>17</sup> Mr. Adams's testimony is transcribed at 2 Tr 254-262.

<sup>18</sup> Mr. Tondou's testimony is transcribed at 2 Tr 196-228.

<sup>19</sup> See 2 Tr 286-301.

## MCAAA

Mr. Peloquin testified regarding the company's gas transportation contract for the Zeeland plant with SEMCO Energy.<sup>20</sup> He recommended a disallowance of \$2.3 million, representing the annual payment included in the reconciliation. He testified that the payment is not an allowable Act 304 expense, asserting that the expense is primarily a capital investment. In support of this testimony, Mr. Peloquin reviewed the Commission's April 11, 2000 order in Case No. U-12301, focusing on language characterizing the contract between SEMCO and SEI Michigan, LLC, as an agreement "to construct, own, operate and maintain" a lateral pipeline from ANR to the Zeeland plant. He testified that the charge approved in that order appears designed to recover SEMCO's investment over only 12 years. Mr. Peloquin also testified that the amount paid under the contract is not a reasonable fuel transportation expense. He compared the 24 cents per Mcf transportation charge for the 7.5 mile pipeline to the ANR charge of 14 cents per Mcf for transportation over hundreds of miles, as shown in Exhibit MCAAA-1.

Mr. Peloquin also recommended disallowance of half of the fees paid to gas purchasing agents<sup>21</sup> BP and EDF to supply Zeeland, testifying that Consumers had not reasonably solicited bids for this supply. He testified that the company had unreasonably insisted on obtaining outside gas management services and had also unreasonably insisted on obtaining firm transportation from ANR, while the company had other options it did not explore. He presented a map showing Consumers' service

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<sup>20</sup> Mr. Peloquin is a CPA, and consultant to MCAAA. His testimony is transcribed at 2 Tr 267-282.

<sup>21</sup> The agency agreements were with BP Canada Energy Marketing Corporation (BP) and EDF Trading North America, LLC (EDF).

territory in relationship to gas pipelines and storage fields, and cited discovery responses contained in Exhibits MCAAA-1 and MCAAA-4 in support of his analysis.

Mr. Peloquin also testified regarding the company's coal transportation contracts, objecting to the company's lack of vessel transportation for its western coal, and discussing Detroit Edison's greater use of lake vessels. While he recommended that the Commission encourage the company to maximize its economic use of lake vessel transportation of western coal, he did not recommend a disallowance. He noted that the company is using some lake vessels, as shown in Exhibit MCAAA-3.

MCAAA also presented Exhibit MCAAA-5 and Exhibits MCAAA-8 through MCAAA-13.<sup>22</sup>

### MEC

Mr. Sansoucy also testified regarding the Zeeland plant, taking issue with the reasonableness of the SEMCO contract "demand" charges and transportation costs, and further testifying that the plant was underutilized.<sup>23</sup> Regarding the BP and EDF agency contracts to supply Zeeland, he cited the Commission's decision in the plan case, and concluded that the company had failed to make the required showing that the transportation portion of the agency contract costs was reasonable.

In addition, Mr. Sansoucy took issue with the "demand charge" of \$2.3 million paid to SEMCO, ostensibly for transportation from the ANR interconnection to the Zeeland plant, a distance of 7.5 miles. He compared the plan case forecast cost of

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<sup>22</sup> Proposed Exhibits MCAAA-6 and 7 were copies of Commission orders and were not admitted on that basis that Commission orders need not be made part of the evidentiary record.

<sup>23</sup> Mr. Sansoucy is an engineer, and the owner of his own consulting firm. His testimony is transcribed at 2 Tr 417-429.

\$0.243 per Mcf, shown in Exhibit MEC-4, to the actual 2010 cost of \$0.289 per Mcf. Mr. Sansoucy testified that the cost of gas transportation under the SEMCO contract was greater than the entire cost of the gas management services from EDF, which includes transportation in addition to other services. Referencing provisions of the contract that call for increases at various intervals over the life of the contract, and a \$3 million balloon payment in the last year of the contract with an option to purchase the pipeline for \$1, Mr. Sansoucy testified that a significant portion of the demand charge is payment for purchase of the pipeline. He also cited testimony from Mr. Gallaway in Case No. U-16890, the company's 2012 plan case, indicating that he assumes Consumers will purchase the pipeline.

In testifying that the Zeeland plant was generally underutilized, Mr. Sansoucy relied on Exhibits MEC-5 through MEC-7. He testified that had Zeeland operated as a base load plant for 8 months in 2010, it would likely have generated an additional 1.5 billion kWh.

In addition, he testified regarding the companies purchase volumes of spot and contract coal, taking issue with the company's purchase of a mix of 93.3% contract coal and 6.7% spot market coal, when spot prices were significantly below contract costs. Exhibit MEC-1 summarizes the company's plan and actual contract and spot market coal purchases by source. He referred to Mr. Foster's testimony from Case No. U-15675-R, indicating that the company's procurement practices call for purchases of 70% to 90% contract coal. Reviewing the company's coal contracts, he testified that the company's actual contract purchases were very close to the contract minimum requirements, shown in Exhibit MEC-2:

With the reduced generation requirements in 2010 and the high level of committed long-term contract coal in its purchasing strategy, the Company effectively contracted itself out of the opportunity to reduce its cost with significant spot purchases and ended up giving up most of its flexibility in the marketplace.<sup>24</sup>

Mr. Sansoucy testified that the lack of flexibility in the company's coal contracts had an impact of \$29 million in coal costs compared to contracts with sufficient flexibility to maintain an 80:20 contract-to-spot coal ratio, as shown in Exhibit MEC-3.<sup>25</sup>

He also testified regarding the cost of transmission outages attributable to maintenance activities on the METC system. He testified that two significant transmission system outages resulted in \$17.5 million in congestion charges for Consumers. The outages are described in Exhibit MEC-8. Mr. Sansoucy testified to his opinion that ratepayers should not bear the cost of these outages, which he attributes to Consumers' failure to protect itself contractually in the sale of Palisades, and otherwise failing to minimize the harm done by METC's actions.

MEC also presented Exhibits MEC-10 and MEC-11.

### Staff

Mr. Gerken testified to Staff's analysis of the company's reconciliation.<sup>26</sup> He explained that Staff revised the beginning balance attributable to the underrecovery from calendar year 2009 to \$31,327,545, based on the Commission's June 16, 2011 order in Case No. U-15675-R. Mr. Gerken also explained that Staff revised the 2010 amount included for capped fuel and variable O&M payments to the BMPs to match the recovery amount of \$10,556,059 sought by the BMPs. He further testified that Staff

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<sup>24</sup> See 2 Tr 423.

<sup>25</sup> See Exhibit MEC-3.

<sup>26</sup> Mr. Gerken is an auditor in the Regulated Energy Division of the MPSC. His testimony is transcribed at 2 Tr 308-316.

agrees with the BMPs' request to recover 2010 actual fuel and variable O&M costs of \$10,566,059, but recommends that the Commission reject TES's additional request to recover \$412,918 in NO<sub>x</sub> and SO<sub>2</sub> allowance costs, also citing the Commission's June 16, 2011 decision in Case No. U-15675-R.<sup>27</sup> Staff's reconciliation calculations are presented in Exhibit S-1, showing a cumulative underrecovery of \$11,318,405 with interest through December 2010.

### Rebuttal

The company presented rebuttal testimony from 5 witnesses.

Mr. Gallaway testified only on rebuttal. He addressed Mr. Peloquin's and Mr. Sansoucy's testimony regarding the SEMCO transportation contract, disputing that the contract should be considered a capital lease, and disputing that the contract is unreasonable, asserting that the contract cost per Mcf cannot properly be compared to ANR tariff rates or other transportation costs because it is a fixed contract. Mr. Gallaway also addressed Mr. Peloquin's testimony regarding Consumers' use of an agent to procure, store, and transport gas for Zeeland, asserting that the agent agreements were the product of reasonable competitive bidding.

Mr. Blumenstock testified in rebuttal to Mr. Sansoucy's claim that Zeeland was underutilized during 2010. He testified that MISO determines the utilization of Zeeland based on an industry-accepted economic dispatch analysis. He also testified regarding assumptions underlying the company's study of Zeeland as a base load plant, contending that more realistic assumptions would reduce the net revenue from operating the plant for a positive \$8.8 million to a negative number, and testifying that

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<sup>27</sup> See 2 Tr 312-316.

operating Zeeland as a cycling plant produced net revenue of \$10.3 million during the 2010 PSCR year. Additionally, he took issue with Mr. Sansoucy's calculation of the likely Zeeland generation and the amount of coal that could have been displaced had Zeeland operated as a base load plant.

Mr. Foster testified in rebuttal to Mr. Sansoucy regarding the cost of coal and in rebuttal to Mr. Peloquin regarding coal transportation costs. Regarding the balance between the company's purchase of spot coal and contract coal, Mr. Foster testified to the company's purchasing strategy and the risks associated with reliance on the spot market. He presented Exhibits A-25 and A-26, identifying the coal contracts in place in 2010 along with actual purchases and receipts, and took issue with Mr. Sansoucy's estimates of the flexibility provided in those coal contracts. Regarding the cost of coal transportation, he testified that the company does transport some coal by water, but that market conditions and the physical location of the company's plant do not justify greater reliance on vessel transportation.

Mr. Ronk testified in rebuttal to Mr. Sansoucy's testimony regarding transmission outages. He testified that the outages were scheduled by METC, not the company, and explained the company's actions to minimize the congestion costs associated with the outages through the acquisition of "Financial Transmission Rights", or FTRs. He also testified regarding difficulties associated with acquiring FTRs given market conditions and the lack of notice of one of the outages.

Mr. Clark also testified in rebuttal to Mr. Hasselman's testimony regarding the transfer price. He testified that the company determined the transfer price and transfer cost in accordance with prior Commission decisions. He further testified that Mr.

Hasselman's proposed transfer price calculation erroneously excluded a capacity value, uses real-time rather than day-ahead LMP prices, and uses average LMPs that do not reflect the variation in off-peak and on-peak energy deliveries by resource.

Staff presented Mr. Harlow's rebuttal testimony addressing Mr. Hasselman's analysis.<sup>28</sup> Mr. Harlow testified that the transfer price calculation required by Act 295 is not exclusively based on the LMPs, and is not intended to be reconciled or trued-up to actual LMPs. Additionally, he cited the Commission's June 16, 2011 order in Case No. U-15675-R as clarifying that PSCR reconciliation proceedings are not a forum for revising transfer prices.

### Briefs

The parties take positions on briefs that are generally consistent with the testimony of the witnesses they presented. Consumers requests that the Commission approve its reconciliation with the modifications made by Staff, as presented in Exhibit S-1, with the refund procedure proposed by the company; Consumers does not take a position on TES's request for recovery of NO<sub>x</sub> and SO<sub>2</sub> costs above the capped amounts.

MEC argues that Consumers has not shown the reasonableness and prudence of the costs to supply and transport gas to the Zeeland plant.<sup>29</sup> MEC further argues that the plant was underutilized. And MEC argues that the congestion costs associated with

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<sup>28</sup> Mr. Harlow is a public utilities engineer in the Electric Reliability Division of the MPSC; his testimony is transcribed at 2 Tr 317-323.

<sup>29</sup> MEC does not argue for a disallowance based on Mr. Sansoucy's testimony that the SEMCO pipeline costs reflect capital costs that are not recoverable PSCR costs.

METC transmission system maintenance outages should not be passed on to ratepayers.

MCAAA argues that the SEMCO pipeline charges should be disallowed, and takes issue with the fees paid under the company's agency agreements to supply the Zeeland plant. MCAAA also argues that the company has not adequately evaluated its coal transportation options, including greater reliance on lake vessels to transport coal.

The Attorney General argues that the Commission should revise its treatment of the transfer price calculation and adopt Mr. Hasselman's analysis. The Attorney General also opposes recovery of NO<sub>x</sub> and SO<sub>2</sub> costs by TES. In its reply brief, the Attorney General also reviews certain arguments of the parties regarding the cost and dispatch of Zeeland, but does not request any specific relief.

Staff supports the reconciliation calculations presented in Exhibit S-1. Staff argues that the Commission should deny recovery of NO<sub>x</sub> and SO<sub>2</sub> costs by TES. Staff also opposes the Attorney General's transfer price calculations and requests that the Commission reconsider its prior decisions.

Because no party disputes the BMPs request for recovery of fuel and variable operating expenses subject to the cap under MCL 460.6a(8), the BMPs' briefs primarily focus on TES's request to recover NO<sub>x</sub> and SO<sub>2</sub> costs. Staff and the Attorney General argue in opposition to this request.

The positions of the parties, and the record evidence on the disputed issues, are discussed in more detail below.

### III.

#### DISCUSSION

##### A. Zeeland costs

In the plan case, Consumers projected a cost of 54 cents per MMBtu above NYMEX prices for transporting gas to the Zeeland plant.<sup>30</sup> In its plan case decision, the Commission reviewed claims that Consumers had failed to support this cost projection:

The Commission further agrees that Consumers has not proven that the 54 cents per MMBtu for transportation expense is reasonable and prudent. The Commission will not, however, adjust the plan factor in this proceeding but will require Consumers to support the transportation cost during reconciliation.<sup>31</sup>

On this record, the parties agree that there are two components to the company's cost to supply gas to the Zeeland plant, which totaled approximately 56 cents per MMBtu for the 2010 plan year. One component is an agency fee covering the purchase of gas, transportation on the ANR pipeline, and storage. The company had two agency contracts during the plan year providing this service. The second component comes from a contract with SEMCO to transport gas from the ANR pipeline to the Zeeland plant. MCAAA and MEC challenge both components, as discussed below. The SEMCO contract is discussed in section 1; the agency contracts are discussed in section 2.

##### 1. SEMCO contract

Consumers assumed the SEMCO contract when it acquired the Zeeland plant. Originally, SEMCO contracted to construct, own, and operate a 7.5 mile pipeline from

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<sup>30</sup> The parties generally agree that MMBtu and Mcf can be used interchangeably in discussing the issues in this reconciliation.

<sup>31</sup> See February 22, 2011 order, Case No. U-16045, page 12.

ANR to the Zeeland plant for the plant's former owner, SEI Michigan, L.L.C., an independent power producer. The Commission approved this contract in its April 11, 2000 order in Case No. U-12301. Under the contract, which is Exhibit MCAAA-5 in this proceeding, Consumers pays a fixed demand charge as set forth in the contract each year until the year 2012, when a "balloon payment" of \$2,995,000 is due and Consumers has the option to purchase the pipeline for \$1.<sup>32</sup> Should Consumers choose not to purchase the pipeline in 2012, it can extend the contract term by five or ten years. Under either of those options, it does not make the balloon payment of \$2,995,000, and the annual fixed payments fall to \$700,000 for the five-year extension or \$590,000 for the ten-year extension. At the end of either extension period, the company again has the option to purchase the pipeline.<sup>33</sup>

MCAAA and MEC argue that the Commission should disapprove the \$2.3 million payment for 2010 attributable to the company's contract with SEMCO.

MCAAA contends that the SEMCO contract payments include capital costs associated with purchasing the pipeline. Both Mr. Sansoucy and Mr. Peloquin testified that the fixed annual charge under the contract should be considered a capital cost not recoverable as a PSCR cost.<sup>34</sup> Mr. Sansoucy testified: "It is apparent from these circumstances that a significant portion of the annual demand charge is an installment

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<sup>32</sup> The amount of the demand charge varies by contract year as provided in Article 7 of the contract. 2010 is year 10 of the contract, and the annual demand charge in years 8 through 12 of the contract is \$2,295,000.

<sup>33</sup> Under the five-year extension, the company has the option to purchase the pipeline for a balloon payment of \$1 million, plus \$1. Under the ten-year extension, the annual demand charge rises to \$790,000 for the last five years, but no balloon payment is due and the company again has the option to purchase the pipeline for \$1. Additionally, should the company purchase the pipeline, SEMCO retains the right to match any offer to operate and maintain the pipeline solicited from a third party.

<sup>34</sup> See 2 Tr 424-426; 2 Tr 273-276.

payment toward the ultimate purchase of the pipeline.”<sup>35</sup> Mr. Peloquin testified to his opinion that the demand charge includes capital costs:

Reading the U-12301 order in context, I believe the \$2,295,000 annual charge is designed to recover SEMCO’s investment over 12 years. Charging the ratepayers for a long-lived utility asset over only 12 years is not good ratemaking policy.<sup>36</sup>

MEC argues that the company has failed to support the reasonableness and prudence of the SEMCO “demand charge”, arguing that the “sheer cost” of the transportation service is excessive when compared to the cost of transportation on the ANR pipeline over much greater distances.<sup>37</sup> MCAAA likewise argues that the company has failed to support the reasonableness of the pipeline charges. Mr. Sansoucy compared the 28.9 cents per Mcf SEMCO cost to the 27 cents per Mcf cost paid under the agency contracts with BP and EDS, arguing that the lower agency contract costs cover the transportation of gas on the ANR pipeline system as well as the other gas management services provided.<sup>38</sup> Mr. Peloquin made a similar comparison, comparing the SEMCO charge to the average ANR pipeline charge of 14 cents per Mcf, which he testified covers distances that average hundreds of miles.<sup>39</sup>

Consumers asserts that the contract payments do not include capital costs, citing Mr. Gallaway’s rebuttal testimony that the pipeline is not an asset of the company, and that the pipeline is not in rate base:

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<sup>35</sup> See 2 Tr 425.

<sup>36</sup> See 2 Tr 276.

<sup>37</sup> Based on Mr. Gallaway’s testimony on cross that the company is declining to purchase the pipeline in the 12th year of the contract, MEC has dropped a claim that the contract payments include capital payments for the pipeline acquisition. MEC indicates that the reasonableness and prudence of the company’s decision not to purchase the pipeline can be reviewed in the 2012 PSCR plan case. See MEC’s brief, page 4.

<sup>38</sup> See 2 Tr 424-425.

<sup>39</sup> See 2 Tr 275; and see Exhibit MCAAA-1, page 1, showing various pipeline rates.

[T]he Company has made no capital investment with regard to the SEMCO lateral pipeline and it does not have any ownership right or claim to any portion of the pipeline as an asset of the Company. The SEMCO pipeline is not part of or included in the Company's electric (or gas) rate base.<sup>40</sup>

In its reply brief, the company also argues that since it has not purchased the pipeline, the expenses incurred are not capital expenses.

Regarding the reasonableness of the costs, Consumers relies on Mr. Gallaway's and Mr. Blumenstock's rebuttal testimony in arguing that the SEMCO charges are reasonable and prudent.<sup>41</sup> Consumers argues that it is not appropriate to evaluate the per-Mcf cost of the pipeline, because the company pays a fixed annual cost that does not vary with the volume transported, within the contract limits.<sup>42</sup> Consumers argues that comparing the cost of the SEMCO contract per Mcf transported to the cost of firm transportation on ANR or to the company's estimated agency fees under the BP and EDF contracts is not a valid comparison because the SEMCO contract payment is a fixed charge. In this context, Consumers argues that the SEMCO contract permits it to transport up to 67,890,000 Mcf annually; using this volume rather than the planned 2010 Zeeland volume of 9,462,754 Mcf, or the actual 2010 Zeeland volume of 7,949,781 Mcf, results in a per-Mcf cost of only 3.4 cents per Mcf.

Turning first to the question whether the lease payments include capital costs, MCL 460.6j(13)(d) directs the Commission in a power supply cost recovery reconciliation to: "Disallow transportation costs attributable to capital investments to develop a utility's capability to transport fuel or relocate fuel at the utility's facilities and disallow unloading and handling expenses incurred after receipt of fuel by the utility."

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<sup>40</sup> See 2 Tr 438.

<sup>41</sup> See Consumers' brief, pages 7-9, 12-14, 18-20; reply brief, pages 5-6, 9-10.

<sup>42</sup> See Gallaway, 2 Tr 439-441.

The provisions of the SEMCO contract cited by MCAAA, along with Mr. Peloquin's and Mr. Sansoucy's testimony, raise a legitimate concern that the pipeline contract is designed to allow SEMCO to fully recover the costs of the pipeline over a 12 to 22 year period of time, without regard to the expected useful life of the pipeline.

Although Mr. Gallaway characterizes the contract terms as "simple and unambiguous",<sup>43</sup> the contract cannot be characterized as a "simple" gas transportation agreement. For example, the contract quantities do not change<sup>44</sup> but the annual fee varies significantly over the initial term of the agreement (\$1,295,000 in Year 1; \$995,000 in Years 2 through 5; \$1,495,000 in Years 5 through 7; \$2,295,000 in Years 8 through 12), and if the agreement is extended beyond 2012, the annual fee falls from the 2010 charge of \$2,295,000 to \$700,000 with a five-year extension, or \$590,000 with a ten-year extension.<sup>45</sup> If the term is not extended, a balloon payment of \$2.9 million is also due in year 12, whether or not the pipeline is purchased for \$1. If the term is extended five years, the balloon payment at the end of that period is \$1 million, and the pipeline may be purchased for \$1. If the term is extended for ten years, there is no balloon payment, and the pipeline may be purchased for \$1.<sup>46</sup>

Should Consumers purchase the pipeline at any of the purchase points, and should Consumers then decide to use a third party to operate the pipeline, SEMCO has the right to match any bid received for that purpose.<sup>47</sup> Also, note that under the

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<sup>43</sup> See 2 Tr 437.

<sup>44</sup> The Maximum Daily Quantity (MDQ) is 186,000 MMBtu per day, as set forth in Article 1 of the contract, page 3, in Exhibit MCAAA-5.

<sup>45</sup> See Exhibit MCAAA-5, Article 7, pages 12-13.

<sup>46</sup> See Exhibit MCAAA-5, Article 10, pages 16-18.

<sup>47</sup> See Exhibit MCAAA-5, Article 10, paragraph 10.3.

agreement, SEMCO is obligated to pay any taxes, including taxes associated with ownership, that might be assessed to Consumers.<sup>48</sup>

Additionally, some of the key provisions of the contract cannot be interpreted without reference to another agreement, referred to in the contract as the “Lateral agreement”. The Lateral agreement is referenced in Article 7 in identifying the annual demand charges,<sup>49</sup> and in Articles 2 and 14 in defining Consumers’ rights in the event of a default.<sup>50</sup> The Lateral agreement is not a part of the record in this case.

Citing Mr. Gallaway’s testimony, Consumers identifies two factors to show that the contract payments should not be considered in part as purchase payments. First, the company argues it does not own the pipeline. This does not squarely address the question whether payments made under the agreement are in part payments to acquire the pipeline. Clearly the law recognizes the concept of a capital lease that does not initially transfer ownership of the subject property. For example, the tax treatment of capital leases can differ from the tax treatment of operating leases.<sup>51</sup>

Second, Consumers argues that the pipeline is not in Consumers’ rate base. But capital leases are generally not included in rate base, as the Commission indicated in its Mich Con rate case decision in Case Nos. U-10149 and U-10150.<sup>52</sup>

This PFD finds that the company’s generalized rebuttal testimony is not persuasive in response to Mr. Peloquin’s and Mr. Sansoucy’s testimony. Consumers

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<sup>48</sup> See Exhibit MCAAA-5, Article 7, paragraph 7.2, page 13.

<sup>49</sup> See Exhibit MCAAA-5, Article 7, paragraph 7.1a, page 13.

<sup>50</sup> See Exhibit MCAAA-5, Article 2, paragraph 2.3(a), pages 4-5, and paragraph 14.1(d), page 23.

<sup>51</sup> See, e.g., *Cargill Inc v United States*, 91 F Supp 2d 1293 (D Minn 2000).

<sup>52</sup> See October 28, 1993 order, Case Nos. U-10149 and U-10150, page 19 (“Because the Commission does not permit their explicit inclusion in the utility’s rate base and capital structure, capital leases should not be implicitly included in a utility’s capital structure as proposed by Mich Con.”)

has the burden to establish that the costs it seeks to recover in this reconciliation meet the statutory criteria for recoverable PSCR costs. Consumers has failed to establish that the SEMCO contract payments reflect only transportation costs rather than the additional capital costs of acquiring the pipeline. Because capital costs to develop a utility's capability to transport fuel are not recoverable under MCL 460.6j(13)(d), this PFD recommends that the Commission exclude the \$2.9 million SEMCO payment, or in the alternative, give Consumers Energy the opportunity to demonstrate the estimated portion of the lease payment that should be considered a capital payment and the estimated portion that should be considered to cover operation and maintenance of the pipeline.

Turning next to the question of the overall reasonableness of the company's use of the SEMCO pipeline to supply gas to Zeeland, based on the foregoing discussion, this PFD does not find that the pipeline payments are unreasonable or imprudent. When the company assumed the contract following the Commission's decision in December of 2007, it would have been approximately the 8th year of that contract. At that point, consistent with the conclusion that the lease payments were in part capital payments covering eventual purchase of the pipeline, the contract assumed by Consumers reflected substantial investment in the pipeline.

## 2. Agent services contracts

During 2010, Consumers relied on contracts with BP Canada Energy Marketing Corporation (BP) and EDF Trading North America, LLC (EDF) to supply gas to the ANR/SEMCO interconnection for use at the Zeeland plant. The company characterized

these contracts as “all-inclusive” or “all-in” contracts, with the gas marketing agents supplying commodity, transportation, storage, and delivery of the gas.<sup>53</sup>

Mr. Blumenstock testified that Consumers used the agents to take advantage of their existing firm transportation and storage rights on ANR, and their gas procurement expertise.<sup>54</sup> He testified that the agent contracts were competitively bid in 2007 and 2009, with the lowest bidder selected. Each contract calls for the agents to deliver gas to the ANR interconnection point between the ANR pipeline and the SEMCO pipeline discussed above. He testified that under each contract, Consumers paid only for gas actually delivered, and that prices were based on published indexes, with adders that varied by the timing and volume of purchases.

Mr. Peloquin testified to his opinion that the company did not adequately consider other alternatives to firm ANR transportation to supply Zeeland, using a map of Consumers’ service territory, storage, and transmission fields (Exhibit MCAAA-2) to indicate that the company had alternatives such as a lateral from its own gas transmission system or storage fields to the plant. He further questioned whether the company could use the ANR firm transportation contract in place to supply its natural gas customers.<sup>55</sup> He also testified that the company did not obtain a meaningful number of bids:

Consumers solicited bids for a gas management contract in 2007 and 2010 for the gas supply applicable to Zeeland. Based upon Consumers discovery responses, Consumers apparently received two bids in 2007 and one in 2010. One of the 2007 bids was rejected because it did not include firm ANR transmission. When you set the bid specifications so high that only huge oligopolistic gas traders who have locked up ANR’s firm

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<sup>53</sup> See Gallaway, 2 Tr 442.

<sup>54</sup> 2 Tr 329-332.

<sup>55</sup> See 2 Tr 278-279, Exhibit MCAAA-1.

transportation are eligible, you do not have effective competition. Consumers numerous statements that the Zeeland gas supply was competitively bid is absurd and disingenuous.<sup>56</sup>

Mr. Sansoucy testified that the company failed to comply with the Commission's directive in the plan case requiring the company to support its transportation costs in the reconciliation. He testified that the company did not identify the portion of the agency contract costs that covered transportation on ANR.<sup>57</sup>

In rebuttal, Mr. Gallaway testified that the choice of firm transportation was reasonable, to support the company's ability to bid the Zeeland plant into the MISO market.<sup>58</sup> He further testified that the bidding was more competitive than described by Mr. Peloquin. He asserted that for the 2007-2010 contract awarded to BP, the company solicited bids from 10 companies, received five bids, and removed two of those bids because they did not meet the bid specifications. Likewise, for the 2010-2013 contract awarded to EDF, he testified that the company solicited bids from 17 companies, and received four bids. Regarding the availability of alternatives to the use of an agent with firm transportation on ANR, Mr. Gallaway testified that the company's existing contract with ANR was intended for its gas customers, and does not have enough volume to serve the Zeeland plant. Finally, he testified that in comparison to building its own transportation and storage, the company would pay the cost of those services whether or not they were used.

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<sup>56</sup> See 2 Tr 277.

<sup>57</sup> See 2 Tr 426.

<sup>58</sup> See 2 Tr 443-449.

MCAAA recommends a disallowance of half of the fees paid to the agents under these contracts in 2010.<sup>59</sup> MCAAA relies on Mr. Peloquin's testimony, and argues that Consumers failed to establish that the fees are reasonable and prudent in response to the Commission's express ruling in the plan case, that in entering these agreements Consumers failed to explore alternatives to an "all-in" contract, including arranging for the purchase, delivery, and storage of gas itself, and that a disallowance is necessary to instill in Consumers a duty to minimize its costs. MCAAA also objects to the company's failure to identify the total amount of fees paid to the agents during the PSCR year. MCAAA presented discovery responses from the company in Exhibits MCAAA-4 and MCAAA-9 through 12.

MEC also recommends that the Commission disallow all or a portion of the agency contract costs, also concluding that the company has failed to support the reasonableness and prudence of the contracts although the Commission expressly required the company to do so.<sup>60</sup> MEC argues that the company has not separately identified the transportation cost component embedded in the price of gas, and has provided no new information regarding these contracts in this record relative to the plan case record.

Consumers' brief relies on Mr. Blumenstock's and Mr. Gallaway's testimony. Consumers argues that the contracts were competitively bid, and the company chose the lowest bidder.<sup>61</sup> The company also argues in response to Mr. Peloquin's analysis that he was mistaken regarding the number of bid solicitations and bidders involved in

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<sup>59</sup> See MCAAA's brief, pages 15-26.

<sup>60</sup> See MEC's brief, pages 8-10.

<sup>61</sup> See Consumers' brief, pages 7-8.

the company's competitive bidding, asserting that for the most recent EDF contract, bids were solicited from 17 providers and 4 of them submitted bids.<sup>62</sup> Consumers also argues that it needed firm transportation on ANR, and did not consider constructing its own pipeline or using its own storage as an alternative to the ANR firm transportation because it was committed to the SEMCO contract to provide transportation from the ANR pipeline to the Zeeland plant.<sup>63</sup> In its reply brief, the company also argues that MEC and MCAAA do not identify what information is missing from the company's presentation. Further, the company argues that MCAAA neglects to account for the additional infrastructure that would be needed to eliminate use of the agent.

MCAAA argues in its reply brief that the bid terms were limiting, and that the company's own rebuttal shows that the bid evaluations were conducted with regard to only 2 to 4 bidders, which MCAAA argues is insufficient.

This PFD recommends that the Commission accept the company's payments under the agency agreements as reasonable and prudent. As noted above, at the time the company purchased the Zeeland plant, and assumed the SEMCO contract, the contract was in its 8<sup>th</sup> year, representing substantial capital investment in the pipeline. It seems reasonable that Consumers chose to utilize the pipeline it was obligated to pay for, and reasonable to conclude the company needed firm transportation on the ANR pipeline. This PFD also finds that the company reasonably engaged in competitive bidding to provide service for the Zeeland plant. As the SEMCO pipeline contract demonstrates, the capital costs associated with the infrastructure required to provide alternative service would not be trivial. Nor could they be developed within a short time

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<sup>62</sup> See Gallaway at 2 Tr 444-445; also see Exhibit MCAAA-10, pages 045R1213-1214.

<sup>63</sup> Also see Exhibit MCAAA-9, page 045R1082.

frame. It was not unreasonable for Consumers to fail to undertake a formal study of the total cost of replicating storage and pipeline capacity to provide equivalent firm service to Zeeland prior to entering into the agent service agreements.

As a caveat, however, the Commission should be concerned that the company is unaware of or oblivious to the total cost of the agent agreements relative to the cost of gas. Mr. Foster identified the variables used to determine the total fees the agent receives for each purchase, but testified that although he reviews the bills for each individual purchase, the total payments to each agent had not been computed.<sup>64</sup> Information regarding the contributing factors to the company's total cost under the current agent contract would appear to be useful, if not necessary, to determine how best to solicit future bids and to evaluate alternatives. For example, the company should expect to know the percentage of volumes purchased for Zeeland "timely" or at least one day in advance, rather than on the day of delivery.

B. Zeeland plant utilization

As noted above, Mr. Sansoucy testified that the Zeeland plant was underutilized during 2010, asserting that the plant ran at an 11% capacity factor, and burned 16% less gas than forecast in the plan case. He reviewed the company's study of the potential for utilizing Zeeland as a base load plant:

The results of the study are summarized again in Exhibit MEC-6 . . . The study demonstrated that the plant would have generated approximately 3.7 billion kWh of electricity if dispatched in each month of 2010 as a base load plant. The study also showed that the plant would have operated profitably for eight of twelve months and would have produced \$15,924,888 of profit. Exhibit MEC-7 is a summary of these facts. It shows that if the plant had run base loaded for the eight months of

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<sup>64</sup> See Foster, 2 Tr 511-531, 518 ("[I]ntraday purchases have a higher added").

profitability, the plant would have generated approximately 2,640,000,000kWh. The actual production was 955,000,000 kWh based on the cured mode of operation for Zeeland.

If Zeeland were base loaded, additional costs would come down on a per-unit basis, such as the SEMCO demand charge, the gas services contract fees, and any other fixed costs related to Zeeland impacted by production. In operating as a base loaded plant for the 8 profitable months in 2010, Zeeland would likely have contributed 2.64 billion kWh generated, and would have displaced approximately 1,430,000 tons of coal. Exhibit MEC-7 shows that at the average per ton price in the PSCR reconciliation of \$46.728 per ton, the coal cost savings can be estimated at \$66,821,000. (This number could conceivably be offset by some amount of MISO sales of energy by the coal units.)<sup>65</sup>

In rebuttal, Mr. Blumenstock testified that MISO is responsible for dispatching the Zeeland plant, using industry accepted economic commitment and dispatch analysis. He further testified that the company's study does not support operating Zeeland as a base load plant:

First, the subject study was never intended to be a detailed, direct comparison of base load operation versus cycling operation. Rather, the study was meant to provide an indication of the high-level economic merit of base load operation over an annual period. Second, the study was based on aggressive assumptions heavily favoring base load. . . .

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The Company concluded that even with assumptions heavily favoring base load operation, operating the combined cycle portion of the Zeeland Plant as a cycling resource was the correct economic choice for 2010. According to the study, base load operation of the combined cycle portion of the Zeeland Plant in 2010 would have resulted in estimated net revenue of only \$8.8 million. Cycling operation of the combined cycle portion of the Zeeland Plant in 2010 resulted in actual, net revenue of \$10.3 million.<sup>66</sup>

Mr. Blumenstock identified the aggressive assumptions as follows: the study assumed an infinite ramp rate, i.e. that Zeeland could instantaneously dispatch between

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<sup>65</sup> See 2 Tr 427.

<sup>66</sup> See 2 Tr 340-341.

maximum and minimum power; the study assumed no risk adder to the incremental offer; the study did not account for increased maintenance costs resulting from base load operation; the study did not include market price deflation as a result of running a generator out of economic order; the study assumed the Zeeland plant would have a 100% availability, with no planned or unplanned outages; and the study did not account for MISO market charges such as Revenue Sufficiency Guarantee charges that occur due to normal operation of a generator.<sup>67</sup> He testified that if the study more accurately modeled the base load operating costs and risks, the estimated net revenue from the combined cycle operations would be significantly less than the \$8.8 million reported in the study.<sup>68</sup>

Mr. Blumenstock also took issue with Mr. Sansoucy's calculations of the impact of increased Zeeland operations, asserting that the combined cycle portion of the plant produced only 663,402,000 kWh during the identified eight-month period rather than 955,000,000 kWh, and that this would have offset 1,021,000 tons of coal, at a value of \$47.8 million, rather than 1,430,000 tons valued at \$66,821,000 as Mr. Sansoucy estimated.

MEC argues in its brief that Consumers failed to dispatch Zeeland reasonably and prudently.<sup>69</sup> MEC argues that the plant was used at only an 11% capacity factor in 2010, well below the plan-case forecast. In addition, MEC argues that the plan-case forecast assumed lower prices of coal and higher prices of gas. MEC interprets the company's study as showing that it would have been profitable to run Zeeland as a

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<sup>67</sup> See 2 Tr 341-342.

<sup>68</sup> See 2 Tr 343.

<sup>69</sup> See MEC's brief, pages 10-16.

base load plant for 8 of 12 months, citing discovery responses presented in Exhibit MEC-6 and MEC-7.

MEC addresses Mr. Blumenstock's rebuttal testimony challenging the estimates Mr. Sansoucy used for the potential Zeeland plant production operated in this manner, and for the coal tonnage and coal cost displaced. MEC argues that Zeeland would still have been profitable even accepting Mr. Blumenstock's estimate that as a base load plant over the eight months at issue, Zeeland would have generated 2.55 billion kWh rather than 2.64 billion kWh. MEC also accepts the company's analysis indicating that the savings from coal displaced by the greater Zeeland operation would be \$47.8 million. MEC argues that Mr. Blumenstock's estimate of a net revenue of \$8.8 million from base load operation, including all months of the year, does not compare to the company's estimate of a net revenue of \$10.4 million from cycling operation, because the \$10.4 million estimate excluded the month of October, in which the cycling plant operations showed an estimated loss:

That is not a comparison of equivalents. A comparison of equivalents would have been base load operation for the profitable months compared with cycling operation for the profitable months. Those numbers were \$15,624,889 for base load operation compared with \$10,369,112 for cycling. Another comparison of equivalents would have been base load operation for all months compared with cycling operation for all months. We do not know what the latter comparison would have indicated, because we do not know the amount of negative revenue under cycling operation in October.<sup>70</sup>

MEC also challenges Mr. Blumenstock's testimony that the assumptions used in the company's initial analysis aggressively favored base load operation, and that revising these assumptions would further weaken the case for base load operation.

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<sup>70</sup> See MEC's brief, page 14.

MEC argues that Mr. Blumenstock's critique of the study assumptions was flawed because it omitted an assumption regarding the cost of gas that would have favored base load operation, and because he erroneously concluded that certain study assumptions favored base load operation. MEC cites Mr. Blumenstock's testimony on cross-examination indicating that if the company used the daily spot price rather than a month-ahead forecast of gas prices, the net revenues would have increased by approximately \$5 million.<sup>71</sup> Regarding the study assumptions, MEC argues that certain of the assumptions Mr. Blumenstock identified, including the infinite ramp rate and the absence of a risk adder, did not favor base load operations because these assumptions were equally used to model cycling operations.

MEC's recommendation based on its analysis of the company's rebuttal testimony is that the Commission disallow \$47.8 million in coal costs based on Mr. Blumenstock's estimate of the value of coal that would have been displaced had Zeeland been dispatched as a base load plant during 8 months of the PSCR year.

In its brief, Consumers relies on Mr. Blumenstock's rebuttal, arguing that the Zeeland plant was not underutilized, and that the company's study of the expected net revenue from running Zeeland as a base load plant did not support the change.<sup>72</sup> In its reply brief, pages 7-8, Consumers characterizes as simplistic the suggestion that Zeeland should have been dispatched more frequently than the plan-case forecast, because coal costs rose and gas costs fell. Consumers argues that MEC's initial brief misrepresents the Zeeland study the company performed, arguing that with realistic assumptions, the study shows that base load operation of the plant would have cost

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<sup>71</sup> See MEC's brief, pages 14-16; Blumenstock, 2 Tr 348-49.

<sup>72</sup> See Consumers' brief, pages 14-15.

more than the revenue it would generate, while cycling operation resulted in net revenue of \$10.3 million.

In its reply brief, Consumers also emphasizes that dispatch of Zeeland is determined by MISO. It argues that MISO requires bids to be submitted on consistent terms. Regarding its study of running Zeeland as a base load plant, Consumers cites Mr. Blumenstock's testimony discussed above, that more realistic assumptions show the plant would have run at a loss compared to running as a cycling plant at a positive net revenue of \$10.3 million in 2010.

Consumers specifically addresses MEC's proposed disallowance of the coal costs that could theoretically have been displaced by running Zeeland as a base load plant. Consumers characterizes MEC's position as "emissions based" rather than based on economic dispatch, and argues that MEC's concern with the environmental impact of the choice is outside the scope of Act 304.

The Attorney General also addressed this issue in his reply brief, arguing that Consumers' arguments are misleading to the extent they suggest that the utility's decisions about when and at what price to bid generation into the MISO market does not have a material effect on MISO's dispatch decisions.<sup>73</sup> The Attorney General argues that MISO's dispatch decisions turn heavily on the availability and price information Consumers provides. The Attorney General further argues that Consumers did not establish that it follows accepted industry practice in bidding Zeeland into the MISO market. The Attorney General does not advocate for any specific relief from the Commission based on this analysis.

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<sup>73</sup> See Attorney General's reply brief, pages 16-17.

This PFD finds that Consumers Energy reasonably relied on the results of its study in deciding not to dispatch Zeeland as a base load plant in 2010. This result is also consistent with the company's 2010 plan to bid Zeeland into the MISO market as a cycling plant. While the study shows base load operations would have been profitable in 8 of 12 months, it is not clear on this record that the profitable months could have been predicted in advance, and if so, with what degree of confidence given the uncertainty associated with key assumptions.

Nonetheless, this PFD recognizes that the study does not establish whether operating Zeeland as a base load plant would be in the best interests of the ratepayers in any future period. Given the importance to ratepayers of an accurate analysis, and the sensitivity of the results to the underlying assumptions, the company should expect to continually evaluate the appropriate bidding strategy to follow for the plant. The company should also expect to refine its analysis, to more accurately capture the costs and risks at issue in changing from one bid strategy to another, and to recognize that the decision can change from month to month, or perhaps week to week, and is not a one-time plan case decision.

While the Attorney General notes that the company did not support its assertion that its bidding matched industry standards, there is no reason to believe the company violated any of the MISO requirements, or otherwise employed bid strategies to reduce the dispatch of Zeeland. Note that the company's treatment of the SEMCO pipeline costs as fixed costs would tend to favor dispatch of the plant.

C. Coal transportation costs

MCAAA cites Mr. Peloquin's testimony to support its argument that the Commission should require the company to present more information regarding its efforts to minimize coal transportation costs in Act 304 cases. MCAAA argues that the record provides scant information as to what steps the company is taking, asserting that the company's western coal is transported on a "bundled basis", so that Consumers does not know how much it is paying for each form of transportation. MCAAA also argues that testimony and discovery responses provided by the company show that the company is not aggressively pursuing lake vessel transportation although such transportation has traditionally been less costly than rail, and although the existence of lake transportation gives the company greater leverage over its rail transportation costs.

In response, Consumers cites Mr. Foster's testimony, and argues that western coal mines are landlocked, requiring transportation to originate by rail, and that not all plants are equipped to handle vessel delivery. Further, the company points to Mr. Foster's testimony that where rail and vessel transportation are both available, the rail transportation is less costly.<sup>74</sup> In its reply brief, the company further responds to MCAAA by arguing that MCAAA has failed to identify the specific information that should be provided.

This PFD recommends that the Commission take no specific action at this point regarding the company's coal transportation costs. For purposes of this reconciliation, MCAAA does not propose a disallowance, and has not refuted the company's more

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<sup>74</sup> See Consumers' brief, page 22.

specific analysis of the economics of rail versus lake transportation. Mr. Peloquin testified regarding discovery information presented by the company as follows:

Consumers response to 16045-MCAAA-CE- indicates that Consumers was using some lake vessel coal transportation beginning in May of 2010. I have attached this interrogatory as Exhibit MCAAA-3. If Consumers is finally making a good faith effort to reduce the transportation cost of its western coal, they should be encouraged.<sup>75</sup>

That the company has bundled rather than separate contracts for rail versus lake transportation does not alone establish that further analysis is called for. The parties to future plan cases can evaluate the company's contracts and other transportation decisions as they are presented for review.

D. METC outages

MEC argues that the Commission should disallow \$15.5 million in net congestion costs incurred by Consumers associated with two METC transmission line outages.

The parties agree on the basic facts. The first outage was due to maintenance work on the transmission lines connecting the Palisades substation to the Argenta substation. As a nuclear plant, Palisades cannot easily reduce its output. Consumers contract to take power from Palisades also does not permit the company to reduce its purchases. On this basis, Consumers incurred congestion charges of approximately \$11.5 million for energy taken from Palisades during the outage.

The second outage was due to maintenance work on transformers serving two substations, Argenta and Gaines. As to this outage, the company indicates it did not get any advance notice prior to the time bidding was due for offsetting FTRs. Although the company nonetheless obtained FTRs that offset \$2.25 million or almost half of the

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<sup>75</sup> See 2 Tr 281.

\$5.9 million in congestion charges associated with that outage, this was part of the company's general FTR decision-making and not specific to this outage.

MEC relies on Mr. Sansoucy's testimony,<sup>76</sup> as well as portions of Mr. Ronk's testimony and Exhibit MEC-8. Regarding the first outage, MEC argues that the congestion costs should be borne by Palisades or by Consumers shareholders, in part on the theory that the company failed to protect itself in its contract with Palisades from these costs. Mr. Sansoucy characterized this as an "oversight in the development of the contractual obligations of the Company in the sale of Palisades."<sup>77</sup> Regarding both outages, MEC argues that METC should absorb the congestion costs caused by its maintenance. MEC points to METC's choice to perform the transformer maintenance work during the peak summer season, and without adequate notice, in the case of the second outage. MEC argues that a disallowance of all or a portion of the congestion costs is appropriate to ensure that Consumers undertakes measures to get METC to address the underlying causes of the congestion costs.

Consumers, relying primarily on Mr. Ronk's testimony, argues that the costs were out of the company's ability to control.<sup>78</sup> Addressing MEC's argument that METC should bear the cost, Consumers argues that FERC sets the terms and conditions of METC's service, and the METC tariff does not permit the company to recover the congestion costs from METC.<sup>79</sup> Addressing the limitations of the company's contract with Palisades, Mr. Ronk testified: "[H]ad a provision been included that would have shifted such costs to the current owners of the plant, the value of the plant would have

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<sup>76</sup> See 2 Tr 427-249.

<sup>77</sup> See 2 Tr 428.

<sup>78</sup> See Consumers' brief, pages 15-16.

<sup>79</sup> See Consumers' reply brief, pages 8-9; Ronk, 2 Tr 79.

been evaluated differently and it is likely that a lower price would have been realized for the plant.”<sup>80</sup>

A review of the parties’ briefs shows that both Consumers and MEC agree that the company’s obligation to minimize its PSCR costs includes minimizing congestion costs associated with transmission. On this record, however, it does not appear that the company failed to take reasonable and prudent actions to minimize these costs.

First, while MEC argues that Consumers should recover these costs from METC, MEC does not dispute Mr. Ronk’s understanding that the applicable tariffs do not permit such recovery. No party expressly addresses the specific tariff language in its brief.

Second, turning to MEC’s argument that the company rather than the ratepayers should bear the congestion costs because the Palisades contract imprudently failed to protect the company from these costs, the contract with Palisades was not comprehensively reviewed in this proceeding. MEC did not refute Mr. Ronk’s testimony that the contract price would likely have been different had the parties shifted risks such as the risk of transmission outages to Palisades. Since contracts generally involve costs and benefits to each contracting party, and are negotiated with those in mind, it is not possible to conclude on this record that Consumers was unreasonable or imprudent in contracting with Palisades. Moreover, the Palisades contract has already been reviewed by the Commission in Case No. U-14992, and the Commission’s order mentioned FTRs in discussing the provisions of the contract.<sup>81</sup>

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<sup>80</sup> See 2 Tr 78.

<sup>81</sup> See March 27, 2007 order, Case No. U-14992, page 13 (“[T]he PPA preserves for Consumers the potential future value from plant attributes not currently traded or valued, and also preserves access to all financial transmission rights (FTRs) associated with the products currently being purchased.”)

Note that MEC does not argue that Consumers unreasonably failed to obtain sufficient offsetting FTRs. Mr. Ronk explained that Consumers did not bid enough to obtain FTRs for the first outage, asserting that the FTRs cleared at a higher price than the company expected for similar outages,<sup>82</sup> but no party has suggested on this record that the company was unreasonable in formulating its bidding strategy. Regarding the second outage, there is also no dispute that the company did not get notice of the outage before the FTR bids were due.

As to MEC's concern that the utility not passively accept METC's cost-imposing maintenance decisions, Mr. Ronk testified that the company is continuing to argue for improved notification of transmission outages.<sup>83</sup> Clearly adequate notice of transmission system maintenance is critical information for the utility. This PFD's recommendation that the Commission approve the congestion costs included in this reconciliation is not intended to deter the utility from pursuing any claims for relief resulting from these outages, or to deter the utility from pursuing measures to protect itself and its customers in the future.

#### E. Transfer prices

Relying on Mr. Hasselman's testimony, the Attorney General argues that the transfer prices should be revised in this PSCR reconciliation to reflect actual LMP prices when those prices are lower than the actual cost of renewable energy over the plan year. The Attorney General acknowledges the Commission orders ruling that the transfer prices established for projects attach for the life of the project, and are not

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<sup>82</sup> See 2 Tr 79; Exhibit MEC-8.

<sup>83</sup> See 2 Tr 76.

revised in PSCR reconciliation proceedings. The Attorney General asks the Commission to reconsider its interpretation and application of MCL 460.1047(2)(b)(iv) and 460.1049(3)(c). Instead, the Attorney General argues that Mr. Hasselman's interpretation is correct, as explained at 2 Tr 290-291, and that the transfer price used in the PSCR reconciliation to reflect the base or "non-incremental" cost of renewable energy should be the actual LMP energy costs, which he testified. Mr. Hasselman recommends a revised transfer price of \$24.64 for the 2009 volumes identified in Exhibit A-4, page 3, and a revised transfer price of \$37.00, based on LMP values provided by Consumers, rather than \$58.13, for the 2010 volumes. On this basis, the Attorney General recommends a reduction in PSCR costs of \$532,052.11.

Staff and the company oppose the Attorney General's recommendation, citing Mr. Harlow's and Mr. Clark's rebuttal testimony and prior Commission decisions.<sup>84</sup>

The Attorney General also argues that accepting the transfer prices already established for Consumers Energy in accordance with the Commission's prior orders, Consumers has still included costs in this PSCR reconciliation that are incremental costs that should be recovered via the renewable energy surcharge and renewable energy plan reconciliation.<sup>85</sup> The Attorney General asserts that the company's PSCR cost summary in Exhibit A-19 includes \$2.7 million in renewable energy purchases, while the transfer price calculation presented by the company calculates total transfer costs of only \$1,255,213. The Attorney General argues that the \$1,480,769 difference should be excluded from the reconciliation.

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<sup>84</sup> See Staff's brief, pages 5-9; Consumers' brief, pages 16-17.

<sup>85</sup> See Attorney General's brief, pages 12-13.

In response, Consumers argues that the Attorney General's calculation is erroneous, that the Attorney General's calculation erroneously excludes the costs presented on line 17 of Exhibit A-19 and includes the costs presented on line 38 of Exhibit A-19 in comparing Exhibit A-19 to Exhibit A-3:

Totaling the correct lines from Exhibit A-19 results in the total correct transfer price amount of \$1,321,605 as shown on Exhibit A-5. Basically, by adding the correct lines from exhibit A-19 and considering the partial year operation of Scenic View Dairy – GP (referred to as Scenic View Dairy – Fennville in Exhibit A-3) as a PA 295 Compliance generator results in a total PSCR expense (or transfer cost) for renewable capacity and energy received pursuant to PA 295 included in this case of \$1,321,605.<sup>86</sup>

Staff concurs, agreeing that the correct lines for calculating the transfer cost from Exhibit A-19 are lines 8, 9, 17, 23, 24, 33 and 57. Staff also indicates that line 23 includes purchases made under the company's Green Pricing Program for most of 2010. Staff also argues that the correct transfer cost to use for comparison purposes from Case No. U-16301 is \$1.32 million, which Staff argues reconciles with the sum of the lines identified above from Exhibit A-19.

This PFD finds that Consumers has adequately explained the potential discrepancy in its presentation, and concludes that the company has not assigned the "incremental" costs associated with renewable energy generation to be recovered in this reconciliation.

F. Biomass Merchant Plant costs

As noted above, the BMPs collectively request recovery of \$10,566,059 in fuel and variable operating costs as shown in Exhibit BMP-1, line 36, and TES also requests

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<sup>86</sup> See Consumers' reply brief, pages 4-5.

recovery of NO<sub>x</sub> and SO<sub>2</sub> allowance costs of \$391,000 and \$21,918 respectively, which it characterizes as fuel costs not subject to the inflation-adjusted \$1 million cap contained in MCL 460.6a(8). None of the parties oppose the BMPs' revised request for recovery of the fuel and variable operating costs shown in Exhibit BMP-1, line 36. Staff, the Attorney General, and MEC contest recovery of TES's NO<sub>x</sub> and SO<sub>2</sub> costs.

MCL 460.6a(8) provides in pertinent part:

The \$1,000,000.00 limit specified in this subsection, as adjusted, shall not apply with respect to actual fuel and variable operation and maintenance costs that are incurred due to changes in federal or state environmental laws or regulations that are implemented after the effective date of the amendatory act that added this subsection.

In support of recovery, Mr. Tondu testified that the NO<sub>x</sub> allowances are fuel costs not subject to the monthly cap under MCL 460.6a(8), asserting that the costs were due to changes in federal or state environmental laws or regulations implemented after October 6, 2008.<sup>87</sup> More specifically, he testified that the NO<sub>x</sub> allowances were purchased to comply with Michigan regulations approved by the EPA on October 19, 2009. He also presented Exhibits BMP-10 and BMP-11. He described Exhibit BMP-10 as a notice from the U.S. EPA to the Michigan Department of Natural Resources and the Environment (MDNRE) stating that the Michigan rules were approved by the EPA on October 19, 2009. He described Exhibit BMP-11 as an email from an MDNRE official asserting that TES was not regulated under the Michigan rules until October 19, 2009, when the revisions to the rules were approved by the EPA.

For SO<sub>2</sub>, he testified that SO<sub>2</sub> allowances were purchased to comply with the federal Clean Air Interstate Rule, which he testified was "implemented" beginning in

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<sup>87</sup> See 2 Tr 212-226.

2010. He further testified that TES was not required to obtain allowances or incur allowance costs prior to October 6, 2008.

Mr. Tondou also testified that the company's decision-making in purchasing the allowances was reasonable and prudent. In support of this conclusion, he testified that TES used a Consumers Energy subsidiary as its agent to acquire the allowances, CMS Energy Resources Management Company, which purchased the allowances along with allowances for its own use with no additional charge to TES.

Staff witness Mr. Gerken relied on the Commission's June 16, 2011 decision in Case No. U-15675-R in recommending that the NO<sub>x</sub> and SO<sub>2</sub> costs be excluded from the reconciliation.<sup>88</sup> Staff's brief similarly relies on this decision.

The Attorney General's initial brief also argues that the Commission's decision regarding NO<sub>x</sub> allowance costs was correct.<sup>89</sup> To the Attorney General, implementation of the MDEQ's rule change in 2007 as a matter of state environmental law did not depend upon approval by the EPA although EPA approval was required before the rules became enforceable as a matter of federal law. Under the Attorney General's interpretation, a change in a regulation is implemented by compliance with the rule making provisions of MCL 24.231 to MCL 24.261.<sup>90</sup> The Attorney General also argues specifically with regard to the SO<sub>2</sub> allowance costs that the applicable federal regulations, part of CAIR, were adopted in 2005, citing Mr. Tondou's testimony at 2 Tr 222.<sup>91</sup>

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<sup>88</sup> See 2 Tr 312-313.

<sup>89</sup> See Attorney General's brief, pages 15-22.

<sup>90</sup> See e.g. Attorney General's brief, page 16.

<sup>91</sup> See Attorney General's brief, page 21; see also Tondou, 2 Tr 222, citing 70 Fed Reg 49721 (August 24, 2005).

In their briefs, the BMPs acknowledge the Commission's ruling in Case No. U-15675-R, and argue in support of cost recovery that the Commission should reconsider its prior ruling on the recovery of NOx costs. The BMPs note the Commission's decision in Case No. U-15675-R was appealed to the Michigan Court of Appeals, and this appeal is still pending. The BMPs further cite to the transcript in Case No. U-15675-R, claiming a deficiency in that record, and also argue that the Commission did not specifically address in its decision how to define "implemented" in MCL 460.6a(8).<sup>92</sup> Regarding the NOx allowances, the BMPs argue in part:

Because the 2007 rules were not the rules due to which TES incurred its environmental costs, the relevant rules are the MDEQ's 2009 rules. Those 2009 rules, as noted above, were promulgated after the statutory cut-off date of October 6, 2008. The 2009 rules were also submitted to the EPA after that date, approved by the EPA after that date, and implemented by the MDEQ after that date. Thus, the costs that were incurred due to those 2009 rules clearly qualify for cost recovery under MCL §460.6a(8).

In summary, the MDEQ's 2007 NOx allowance rules were disapproved by the EPA in 2008 and, therefore, by their terms, had no force and effect at the time when TES incurred its NOx allowance costs in 2009 and 2010. The rules due to which TES incurred its costs were the rules promulgated in 2009. Of course, as detailed in the following section of this brief, the relevant inquiry under PA 286 is not when the regulatory changes were **promulgated**, but, rather, when those changes were "**implemented**". In other words, even if TES had incurred its NOx costs "due to" regulatory changes that were promulgated before October 6, 2008 (which it did not), TES would still have a clear statutory right to recover its 2010 NOx costs if those regulatory changes were "implemented" after October 6, 2008.<sup>93</sup>

Staff and the Attorney General take issue with the BMPs' statutory interpretation in their reply briefs.

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<sup>92</sup> See BMPs' brief, pages 26-29.

<sup>93</sup> See BMPs' brief, pages 45-46 (emphasis in original).

First, regarding the requested recovery of NO<sub>x</sub> allowance costs, this PFD finds that the Commission's decision in Case No. U-15675-R is controlling. The BMPs have not identified any argument presented in this case that could not have been presented to the Commission in Case No. U-15675-R. Although Mr. Tondu presented Exhibits BMP-10 and BMP-11, these exhibits do not shed any additional light on the issue of statutory interpretation, as the Attorney General argues.

Second, regarding the requested recovery of SO<sub>2</sub> allowance costs, the costs arise from regulations adopted in 2005, and no "change" in the applicable laws or regulations implemented after October 2008 is cited as the basis for the costs. As Staff and the Attorney General argue, the BMPs' analysis focuses on when the regulations should be considered to have been implemented, not when "changes" in applicable regulations or laws were implemented. An example of the manor in which the BMPs confuse the implementation of changes in laws or regulations with the implementation of the laws or regulations themselves is shown in the following quotation from the BMPs' brief:

TES was never required to purchase any SO<sub>2</sub> allowances until the new requirements were implemented in 2010. TES did not purchase any SO<sub>2</sub> allowances before 2010 because it was not required to do so. As Mr. Tondu indicated in his pre-filed testimony, 2010 was the first year that TES was required to purchase SO<sub>2</sub> allowances and 2010 was, in fact, the first year that TES did so. Thus, *the implementation of phase 1 of the federal CAIR SO<sub>2</sub> rules* was the sole reason that TES Filer City was required to purchase SO<sub>2</sub> allowances in 2010 and thereafter.<sup>94</sup>

Likewise, in responding to the Attorney General's argument that regarding the manner of implementing changes in laws and regulations, the BMPs argued in their reply brief:

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<sup>94</sup>See BMPs' brief, page 63 (emphasis added).

[The Attorney General's argument at page 16 of his brief] implies that the MAPA contains provisions indicating that rules are implemented when they are promulgated. A review of the statutory provisions cited by the AG, however, reveals that they contain no references whatsoever indicating that the promulgation of a rule is tantamount to the actual implementation of that rule. To the contrary, one of the definitions in section 5 of the MAPA, MCL 24.205(9), states that "promulgation of a rule' means that step in the processing of a rule consisting of the filing of a rule with the secretary of state." This statutory definition makes it clear that promulgation is merely the final administrative step in **processing** a rule. Nothing in the MAPA states that a rule is "implemented" when it is promulgated.<sup>95</sup>

The BMPs' argument that "implementation" should be measured by when compliance with the applicable laws was required writes the word "change" and the phrase "change in" out of the legislation. Under the BMPs' construction, even if no changes were made in the applicable regulations from October 6, 2008 forward, because the applicable regulations did not require TES to take compliance actions until after that date, the regulations were not yet "implemented." Of course, these regulations were adopted sometime, and so would have been a change in comparison to the status quo prior to the regulations, but this construction does not give each word in the statute meaning. That the costs were incurred due to a "change in the law or regulation . . . implemented after the effective date" would equally mean costs incurred due to "a law or regulation implemented after the effective date" under the BMPs' interpretation. For these reasons, this PFD finds that the BMPs have failed to show that the SO<sub>2</sub> allowance costs meet the statutory criteria for recovery above the cap as provided for in MCL 460.6a(8), and recommends that recovery of amounts above the statutory cap be denied.

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<sup>95</sup> See BMPs' reply brief, pages 10-11.

#### IV.

#### **CONCLUSION**

Based on the foregoing discussion, this PFD recommends that the Commission adopt the PSCR reconciliation for 2010 as shown in Exhibit S-1, with the modification that \$2,295,000 million in costs attributable to the company's SEMCO pipeline contract be disallowed, or in the alternative, that the Commission direct the company to establish the amount of the pipeline costs that should be excluded as capital payments toward the purchase of the pipeline. Consistent with Staff's Exhibit S-1, this PFD further recommends that the Commission approve the BMPs' request for recovery of the costs shown on Exhibit BMP-1, line 36, and on Exhibit BMP-2, columns E through G, and deny recovery of the additional \$412,918 requested by TES Filer City.

MICHIGAN ADMINISTRATIVE HEARING  
SYSTEM  
For the Michigan Public Service Commission

Issued and Served:  
June 22, 2012

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Sharon L. Feldman  
Administrative Law Judge